

SOCIAL SECURITY'S ROAD TO INSOLVENCY: A POLICY PROPOSAL TO SAVE THE
NATION'S LARGEST GOVERNMENT PROGRAM

by
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ABSTRACT

Since its inception in 1935, Social Security has been widely regarded as the single most important anti-poverty government program in existence. Serving millions of elderly Americans for over eighty years, Social Security has become a crucial source of income security for a population that would otherwise face potential financial peril. Now the program's trust fund is quickly running out and expected to be depleted by 2034, putting the future of millions of Americans at grave risk. Consequently, and in an effort to address this urgent matter, this capstone project proposes a comprehensive policy package that will attempt to reset the program's finances and make Social Security solvent for future generations. Rethinking the retirement age, the current cap on taxable earnings, and the formula used to calculate cost-of-living adjustments (COLAs) constitute the basis of this proposal, which this project has found to be a potentially effective approach to bring financial soundness back to Social Security.

Advisor: Paul Weinstein Jr., Johns Hopkins University

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DECISION MEMORANDUM

DATE: April 13, 2018

FROM: Cesar Lardies Rivas

TO: SSA Acting Commissioner Nancy Berryhill

SUBJECT: Social Security's Road to Insolvency

Action-Forcing Event

On July 13th of last year, the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance (OASDI) Trust Funds released their annual report on the state of Social Security and the program's future financial prospects. The Board's report indicates that the Social Security trust fund's assets will exceed the program's projected costs every year until 2029, but that the fund's reserves will become depleted in 2034, at which time Social Security income will only be able to pay 77 percent of all scheduled benefits.¹

Statement of the Problem

The 2017 Social Security trustees' report sheds light on the pressing issue of insolvency and what the program's financial struggles could mean for its future and for those Americans looking forward to collecting their Social Security benefits beyond 2034, the expected depletion deadline. As stated in the report, the current pay-as-you-go system, which taxes today's workers and directly transfers the money out as monthly income to Social Security beneficiaries, will allow for only 77% of all scheduled benefits to be payable in 2034. Furthermore, beneficiaries who do receive their scheduled payments beyond that date will likely see major decreases in the total amount of benefits received. According to the Committee for a

¹ Social Security Administration. "The 2017 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds". (July 2017). 23. <https://www.ssa.gov/oact/TR/2017/tr2017.pdf> (accessed January 10, 2018)

Responsible Federal Budget (CRFB), all Social Security beneficiaries are expected to have their benefits cut by 23 percent immediately after the program's trust fund has been exhausted. The CRFB believes that such cut may lead the average retiree to lose \$5,800 in benefits every year.²

The Social Security program has become an important source of stable income for many Americans who have reached old age and retired, but they are not the only beneficiaries. The program also assists millions of disabled Americans under age 65 and those who receive survivor benefits. According to the latest figures published by the Social Security Administration, the total number of individuals currently receiving Social Security benefits is nearly 59 million. Out of this 59 million, 76% are retired Americans of age 65 and older, 13% are disabled and under the age of 65, and roughly 11% represents early retirees and survivors.³ These numbers indicate that an important number of the nation's population relies on Social Security as a source of income and economic security, and many of them could see their livelihoods drastically altered once the current trust fund is depleted.

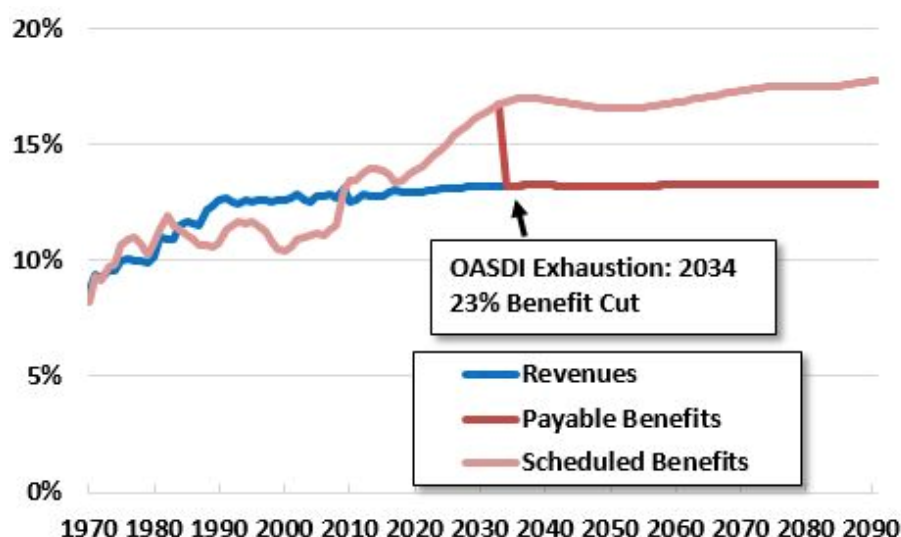
The depletion of the Social Security fund and the subsequent reduction of benefits could have important socio-economic ramifications. Wealthy Americans may not be necessarily in danger if their benefits were to be cut, but an overwhelmingly majority of those who receive benefits from the Social Security Administration (SSA) largely rely on the program as many of them find in their OSASDI benefits their dominant source of income. According to the SSA, 71% of

² Committee for a Responsible Federal Budget. "Analysis of the 2017 Social Security Trustees Report". (July 2017). <http://www.crfb.org/papers/analysis-2017-social-security-trustees-report>. (accessed January 22, 2018)

³ Social Security Administration. "Monthly Statistical Snapshot, December 2017". (December 2017). https://www.ssa.gov/policy/docs/quickfacts/stat_snapshot/. (accessed January 25, 2018)

single elderly beneficiaries and nearly half of elderly married couples receive 50% or more of their annual income from Social Security.⁴

Table 1: Social Security Income and Costs as Percentages of Taxable Payroll



Source: Social Security Administration; Committee for a Responsible Federal Budget

It is important to note that while the current financial state of the OASDI program sees more income coming in than expenditures going out, the future financial prospects of the program tell a different story, as depicted in Table 1. By the end of 2016, Social Security’s total income amounted to \$956 billion, while expenditures were just over \$922 billion. Nevertheless, if we remove interest income from the equation, costs have exceeded income since 2010.⁵ Furthermore, while the current available funds and Social Security’s annual income will be able to cover program benefits through 2033, experts warn against delaying action on this matter. The CRFB has argued that even if immediate action were to be taken, taxes would have to be increased and benefits would have to be cut by considerable

⁴ Social Security Administration. “Fact Sheet: Social Security”. <https://www.ssa.gov/news/press/factsheets/basicfact-alt.pdf>. (accessed January 26, 2018)

⁵ Social Security Administration. “The 2017 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds”. 2.

amounts, and that waiting would only lead policymakers to having to make even more drastic decisions.⁶

History/Background

The financial shortfall of the Social Security program regained special attention in the early years of the 21st century, when it was becoming clear that the number of beneficiaries was growing at a much faster rate than the number of covered workers, a trend that if it was allowed to continue could lead the program into bankruptcy. Table 2 includes a series of projections by the Social Security Administration for the selected time periods (1970-2000, and 2000-2030) that reveal this trend.

Table 2: Projected Percentage Change in Old-Age and Survivors Insurance (OASI) Covered Workers and Beneficiaries

Year	OASI Covered Workers (thousands)	OASI Beneficiaries (thousands)
1970	92,788	22,618
2000	154,624	38,556
2030 (intermediate projection)	184,794	71,547
Percent Change		
1970–2000	66.6%	70.5%
2000–2030	55.0%	85.6%

Source: Social Security Administration

Nevertheless, the future financial status of the Social Security program has been in the minds of experts and policymakers in Washington for decades. While the first forty years of the program’s existence saw a period of continuous expansion, with millions of new workers becoming eligible for Social Security benefits every

⁶ Committee for a Responsible Federal Budget. “Analysis of the 2017 Social Security Trustees Report”.

decade, the 1970s brought about important changes to the socio-economic makeup of the country that would constitute a turning point in the course of the program's history. A change of perspective was underway.

In the early 1970s, Congress approved a sharp increase in Social Security benefits at a time when economic conditions nationwide were especially difficult. Poor economic performance led by stagflation and a global shortage of natural resources placed renewed pressure on the federal government to better administer its limited resources. As a result, this particular scenario brought the financial sustainability of the Social Security program to the attention of policymakers and the public for the first time since its inception. In fact, ever since then the Social Security debate has no longer been primarily focused on the possibility of continuing expanding the program but rather on how to limit its growth and where to locate new sources of revenue for the program in order to guarantee its future.⁷

In response to the growing concern regarding the sustainability of Social Security, the first major large-scale legislative effort to preserve the program occurred under the auspices of the Carter administration in 1977. During that time, Social Security reform had two main objectives: Curb program benefits, and increase revenue in order to make Social Security viable through the year 2030. Previous changes to the program had altered the way benefits were calculated, and up until the 1977 reform benefits were indexed to inflation in order to ensure that benefits would automatically rise at the same rate as inflation. However, this formula was flawed and benefits were in fact rapidly increasing, sometimes at a

7 Patricia Martin & David Weaver. "Social Security: A Program and Policy History". (2005). <https://www.ssa.gov/policy/docs/ssb/v66n1/v66n1p1.html> (accessed February 2, 2018)

speed twice the rate of inflation, at a time when slow economic growth and high levels of inflation made the formula virtually impracticable for extended periods of time.⁸ Thus, the 1977 amendments to the program sought to redesign the benefits formula in an effort to make it more viable. Starting with those becoming eligible for retirement after 1978, the new formula would be indexed to the growth in average wages over the years. This major change improved the program's financial forecast significantly, but it wasn't the only major provision enacted by the 1977 amendments.

The Carter administration knew that they had to slow down the rate at which benefits were growing, but high unemployment and low long-term fertility rates also shed light upon the necessity of increasing revenue sources for the program. As a result, the amendments of 1977 enacted a series of increases in the payroll tax that would go into effect gradually. For employers and workers, the amendments provided for increases in the payroll tax rate, first pushing it up to 6.65% in 1981 and then to 7.65% in 1990. At the time these amendments were signed into law, the Social Security tax rate stood at 5.85%.⁹

These tax hikes were coupled with an increase to maximum taxable amounts on an ad hoc basis, to \$22,900 in 1979, \$25,900 in 1980, and \$29,700 in 1981, after which the base would be automatically adjusted based on average wages. These

8 Patricia Martin & David Weaver. "Social Security: A Program and Policy History".

9 Edward Cowan, "Carter Signs Social Security Tax Rise for 110 Million", The New York Times, (December, 1977) <http://www.nytimes.com/1977/12/21/archives/carter-signs-social-security-tax-rise-for-110-million.html>, (accessed February 6, 2018)

were significant increases to the earnings base considering the fact that in 1977 the maximum taxable amount was \$16,500.¹⁰

The 1977 Carter amendments were intended to keep Social Security financially sound for the next fifty years. Unfortunately, higher-than-expected inflation and lower-than-expected wages in the early 1980s exposed the vulnerabilities of the program, and a renewed concern about the long-term solvency of Social Security began to materialize. Consequently, a new wave of reforms was underway.

In the early 1980s, Americans witnessed the last major overhaul to the Social Security system. Projections at the time indicated that by July of 1983 program revenue from the payroll tax and trust fund assets wouldn't be enough to cover the expenses of the program, making Social Security unable to pay out scheduled benefits.¹¹ Therefore, in an effort to confront the short-term financing crisis engulfing Social Security, the bipartisan National Commission on Social Security was appointed by Congress under the authority of President Reagan in 1981 to study the issue and come up with the best course of action to save the program from bankruptcy.

The NCSS, better known as the Greenspan Commission after its chairman Allan Greenspan, was required to submit its recommendations by January of 1983, and their final findings would become the basis of the 1983 amendments, the last set of major policy changes to the Social Security program to date. Congress largely incorporated the commission's recommendations in March of 1983, which included,

10 Geoffrey Kollmann, "Social Security: Summary of Major Changes in the Cash Benefit Program", Social Security Administration (May, 2000), <https://www.ssa.gov/history/reports/crsleghist2.html> (accessed February 6, 2018)

11 Patricia Martin & David Weaver. "Social Security: A Program and Policy History".

among other things, a gradual increase in the age of eligibility for full retirement benefits, coverage expansion, a delay of the Social Security COLA (cost-of-living adjustment), and an income tax on Social Security benefits for higher-income individuals.

Under these provisions, the age of eligibility for full retirement benefits was to be increased from age 65 to age 66 in 2009 and to age 67 in the year 2027. Also, coverage was extended to federal civilian employees and coverage was made compulsory for all employees of nonprofit organizations. Furthermore, COLA payments were delayed six months and would be payable every January following implementation. Finally, the new income tax on Social Security benefits would tax up to 50% of Social Security benefits earned by higher income recipients, and the revenue gained from this new tax would be automatically transferred to the Social Security trust funds.¹²

The 1983 amendments were successful in addressing the imminent danger the Social Security program found itself in. In the years following the implementation of these provisions payroll taxes and other sources of revenue exceeded the program's costs, leading to a sizable \$1.5 trillion trust fund in the year 2004. However, the Greenspan Commission failed to reach consensus on the long-term fiscal concerns regarding the baby boom generation, the large cohort, nearly 80-million strong, whose members will have reached full retirement age by the year

12 Geoffrey Kollmann, "Social Security: Summary of Major Changes in the Cash Benefit Program",

2031, at which time the beneficiary-to-worker ratio will rise from the current 35 per 100 to 44 per 100.¹³

Although the previous three administrations have, formally or informally, sought to address the future solvency of Social Security, the program has not seen any major legislation comparable to the 1983 amendments in over thirty years. During his 1998 State of the Union address, President Clinton suggested transferring \$2.7 trillion of expected budget surpluses over a 15-year period to the Social Security trust fund in order to extend the program's solvency. While Clinton's plan failed to gain enough political traction to become law, some economists believed that the president's proposal was a bold answer to the program's insolvency that could have maintained scheduled benefits for another 50 years.¹⁴

In May of 2001, President George W. Bush appointed his President's Commission to Strengthen Social Security with three objectives in mind: Preserving the benefits of all retirees, offering personal savings accounts to younger workers, and returning the program to sound financial footing. Despite the president's efforts to enact major reforms during his second term, none of his proposals found the necessary support in Congress to move them forward.¹⁵ Similarly, the Obama administration also pushed for major reforms to the Social Security program. In December of 2011, President Obama's National Commission on Fiscal Responsibility and Reform, also known as the Simpson-Bowles Presidential Commission, proposed a bold plan that combined payroll tax increases and benefit reductions. The

13 National Academy of Social Insurance, "How Will Boomers Affect Social Security", <https://www.nasi.org/learn/socialsecurity/boomers>, (accessed February 8, 2018)

14 Edith Rasell, "Fixing Social Security—The Clinton plan and its alternatives (EPI Briefing Paper)", Economic Policy Institute, (April 1999) https://www.epi.org/publication/briefingpapers_fixsocsec/ (accessed April 5, 2018)

15 Social Security Administration, "Historical Background And Development Of Social Security", <https://www.ssa.gov/history/briefhistory3.html>, (accessed February 9, 2018)

Commission's final plan had several major components, which included increasing the early and normal retirement age to 69 by 2075, including newly hired state and local workers in the program, and increasing the payroll tax cap to cover 90 percent of all wages by the year 2050. Nevertheless, the plan was rejected by commission members as it failed to reach the 14 votes needed to have the blueprint sent to Congress for approval.¹⁶

Today, federal policy regarding the future of Social Security has yet to be more clearly defined and debated by the current administration. President Donald Trump did not address concerns regarding Social Security's future solvency issues during his first State of the Union address last month, and the administration's 2019 budget plan, released on February 12, 2018, does not include any major policy changes to the finances of Social Security.¹⁷

Policy Proposal

Social Security's size, both in terms of its budget and the number of retirees it serves, is a clear indication that applying changes to a single aspect of the program may not be enough to bring about sound and effective reforms. This is why it is important to consider changes to several aspects of Social Security to ensure the program's future financial soundness. Therefore, this memorandum proposes addressing three specific features of the program: Age of retirement, the cap on maximum earnings subject to Social Security taxes, and cost-of-living adjustments.

¹⁶ Lori Montgomery, "The debt fallout: How Social Security went 'cash negative' earlier than expected", The Washington Post, (October, 2011), https://www.washingtonpost.com/business/economy/the-debt-fallout-how-social-security-went-cash-negative-earlier-than-expected/2011/10/27/gIQAcm1QTM_story.html?utm_term=.b8e76317aa6b, (accessed February 9, 2018)

¹⁷ Gregory Wallace, "What's in the Trump budget?", CNN, (February 2018) <https://www.cnn.com/2018/02/12/politics/whats-in-the-trump-budget/index.html>, (accessed February 13, 2018).

Under this proposal, the retirement age to be eligible for full benefits would be raised to 68 (for future retirees only), but it would be done gradually to allow current workers time to plan and adjust to the new system. Starting in the year 2027, when full retirement will stand at 67, the retirement age for those wishing to collect full benefits will be raised by two months every year until it reaches 68 in the year 2033.

This memorandum also proposes raising the cap on wages subject to the Social Security portion of the Federal Insurance Contributions Act (FICA) tax. Currently, the 6.2% payroll tax that employees are responsible for applies to the first \$127,200 of earned wages, up roughly \$10,000 since 2016.¹⁸ This amount should be raised to \$245,000, indexing future increases to average annual wage growth. Naturally, Social Security would pay out additional benefits based on these new taxes since the current benefits formula, which looks at average monthly income in the 35 years with the highest earnings, does not allow any amount above \$127,200 to be included in the calculations.

Finally, this memorandum proposes changes to the way Social Security calculates cost-of-living adjustments (COLAs). Currently, COLA payouts are tied to increases in the Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W). For example, a CPI increase of 2.0% would result in a 2.0% increase in Social Security benefits for any given retiree. This memorandum proposes readjusting the benefits formula so that COLAs continue to be calculated based on the CPI, but indexing them to 1 percentage point below the CPI. That is, a

18 Matthew Frankel, "There's a big change happening to Social Security in 2017 — here's what you need to know", Business Insider, (December 7, 2016), <http://www.businessinsider.com/maximum-social-security-tax-2017-2016-12>, (accessed February 20, 2018)

2.0% CPI increase in a given year would lead to a 1.0% increase in Social Security benefits.

This policy proposal has outlined a roadmap to address Social Security's upcoming financial shortfall. The process by which this new policy would be authorized and implemented by the current administration is presented in the following paragraphs.

a. Policy Authorization Tool

The policy proposal presented here would require important changes to various sections of the Social Security Act. And, considering the scope of these changes, ample consensus would be needed for their successful authorization. Therefore, it would be the responsibility of the United States Congress to authorize these reforms via a new Act of Congress that may be cited as the "Social Security Amendments of 2018" in order to amend currently existing legislation. More specifically, Sections 201, 801, 203(f) of the Social Security Act will be amended to address changes regarding full retirement age, taxable wages, and COLAs respectively.

Considering the fact that the process of amending existing legislation is the responsibility of both the United States Senate and the United States House of Representatives, the current administration should be active in engaging with leadership from the Senate's Committee on Finance and the House's Committee on Ways and Means in order to guarantee successful coordination with the legislative branch.

b. Policy Implementation Tool

Once the United States Congress has authorized the proposed policy, its success will rely on how effectively these changes are implemented by the government. Therefore, the following paragraphs will provide a more detailed description of how this policy would be applied most successfully.

Considering the diverse nature of the different features of the Social Security Act to be addressed by this proposal, effective implementation would require the use of various implementation tools.

First, regulatory enforcement would be needed to implement at least two of the three policy changes included in this proposal. These are the increase in retirement age and the restructuring of the benefits formula as it pertains to the cost-of-living adjustment. Gradually raising the age of full retirement to 68 would be the responsibility of the Social Security Administration as the program's main administrative agency. Nevertheless, and for reasons previously stated, full retirement age would not be raised immediately following authorization. This would be done gradually raising the retirement age by two months every year starting in 2027, when full retirement will stand at 67 years of age, and ending in 2033. By increasing the retirement age, the SSA would simply respond to the fact that Americans are living longer and therefore they are receiving benefits for longer periods than before. The SSA would also be responsible for implementing new regulations on COLA calculations. COLA would continue to be indexed to the annual CPI, but the SSA would be required to calculate COLA benefits by subtracting one percentage point from the CPI. Some analysts have argued that the CPI does not

serve as a true cost of living index as they believe that the current CPI measure overstates cost of living standards, leading to widespread overindexing of federal spending programs like Social Security.¹⁹ COLAs are calculated to ensure that beneficiaries can keep up with inflation, but the current formula may be giving out more benefits than it should, resulting in unnecessary expenses for the program. It is important to note that the Bureau of Labor Statistics, a unit of the United States Department of Labor, is the agency responsible for estimating the CPI for a given year. Therefore, successful implementation of this regulation would require coordination between both agencies so that the appropriate information is available when SSA staff requires it for COLA calculations. The new COLA formula would go into effect the year following authorization so as to not interfere with CPI calculations for the current year.

Finally, the third policy change included in this proposal wouldn't involve regulatory enforcement but rather changes to current tax policy. The 6.2% payroll tax American workers pay into Social Security would remain unchanged, but the cap on the maximum amount subject to taxation would be raised. As of 2017, the cap has been set at \$127,200. This new policy would raise the maximum amount subject to the 6.2% tax to \$245,000. Implementation of this policy would go into effect immediately following authorization and the \$245,000 cap would increase as average wages go up every year thereafter. In this case, it would be the

¹⁹ Michael J. Boskin, "Toward a more Accurate Measure of the Cost of Living", Final Report to Senate Finance Committee from Advisory Commission to Study the Consumer Price Index (December 4, 1996), <https://babel.hathitrust.org/cgi/pt?id=pur1.32754067521926;view=1up;seq=2>, (accessed February 24, 2018)

responsibility of the Internal Revenue Service (IRS) to implement and enforce this new policy.

Regarding the cost of implementing this policy proposal, the current administration wouldn't be facing significant costs. As made evident by the proposal, the ultimate goal of these policy changes is to increase revenue for the Social Security Administration and keep the trust fund financially stable in the long-term. Therefore, with the exception of minor administrative costs related to the initial implementation of the proposal, the administration would be expected to witness significant increases in revenue.

Policy Analysis

Before a decision is made on whether to consider this proposal or not, it is important to first examine the proposal's likelihood of success in achieving its goals as well as the potential risks involved in its application. Therefore, the following pages will offer a through evaluation of the policy proposal by providing an unbiased review of the potential effects, both positive and negative, of all three policy changes suggested in the previous section.

a. Increasing the Retirement Age

Gradually raising the retirement age from 67 to 68 between 2027 and 2033 is undoubtedly the central pillar of the policy proposal. Over the years, much debate and research has focused on the effectiveness of raising the retirement age and how this could help improve Social Security's solvency. According to The Urban Institute, Social Security actuaries estimate that increasing the full retirement age to 68 could

eliminate nearly 29 percent of the program's 75-year funding gap.²⁰ This boost in solvency would primarily be due to the fact that workers would have to continue paying into Social Security for a few more years and the program's income would increase as a result. The proposal's effectiveness may also be based on the fact that Americans today are living longer than before, meaning that they are also drawing Social Security benefits for longer periods of time than ever before. AARP, an interest group which has long advocated for the interests of the elderly and their Social Security benefits, has stated that increasing the program's full retirement age is a "fair and commonsense approach to improving the program's finances". AARP goes on to argue that when Social Security was first implemented back in 1935, 65-year-old men expected to spend about thirteen years in retirement, compared with about eighteen years today. Similarly, women in 1935 averaged fifteen years in retirement and today they spend about twenty years drawing benefits from the system.²¹

The proposal's approach to solving the program's solvency issues may also be regarded as being rather efficient. With virtually no cost to the government, increasing Social Security's full retirement age would have a major impact on reducing the current financing gap, as The Urban Institute's study suggested. Furthermore, there is also historical evidence that this approach could help partially fix Social Security's solvency issues. As a study led by The Brookings Institution's Mark Duggan indicates, the 1983 Social Security amendments, which have been

²⁰ Melissa M. Favreault et al., "Raising Social Security's Retirement Age", The Urban Institute (July, 2010), <https://www.urban.org/sites/default/files/publication/28936/412167-Raising-Social-Security-s-Retirement-Age.PDF> (accessed March 1, 2018)

²¹ AARP, "Updating Social Security for the 21st Century: 12 Proposals You Should Know About", (October 2015), <https://www.aarp.org/work/social-security/info-05-2012/future-of-social-security-proposals.html> (accessed March 1, 2018)

widely discussed in this paper, succeeded in increasing the short and long-term fiscal health of the OASDI program, although much of that success may be attributed to a reduction in overall benefits.²²

The research discussed up to this point offers a description of the effectiveness and efficiency of raising the retirement age and its positive effects on solving Social Security's financial shortfall. Nevertheless, many experts have argued that this proposal could have unintended negative consequences, especially as they relate to the proposal's potential impact on equality.

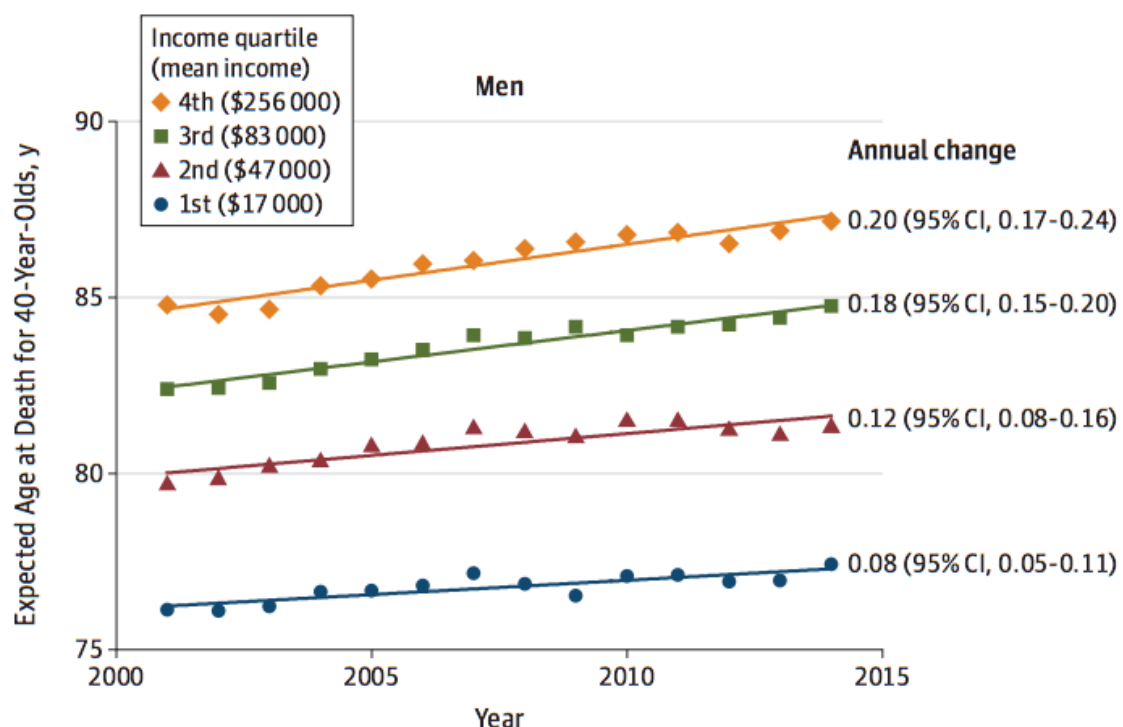
Longer longevity among American workers is often emphasized as the primary reason why increasing the retirement age is needed for securing the future of Social Security. However, many fear that raising the retirement age may have a disproportionate effect on low-income workers. The Heritage Foundation's Romina Boccia believes that lower income populations who are engaged in more labor-intensive types of work "tend to have shorter life expectancies than wealthier recipients".²³ Similar research indicates that low-income, blue-collar Americans have seen negligible gains in life expectancy over the years, a sign that their health is no better than that of low-wage workers born twenty or thirty years ago, suggesting that their capacity to work past age 60 is no better than it was for previous

22 Mark Duggan, "Aching to Retire? The Rise in the Full Retirement Age and its Impact on the Social Security Disability Rolls", The Brookings Institution, (September 2006), <https://economics.yale.edu/sites/default/files/files/Workshops-Seminars/Labor-Public/duggan-061006.pdf> (accessed March 2, 2018)

23 Martha M. Hamilton, "How you would fix Social Security: Raise the retirement age", The Washington Post, (October, 2014), https://www.washingtonpost.com/news/get-there/wp/2014/10/28/how-you-would-fix-social-security-raise-the-retirement-age/?utm_term=.36df2b38f1bb (accessed March 2, 2018)

generations.²⁴ Table 3 offers a visual representation of the existing gap in life expectancy between the rich and the poor.

Table 3: Life Expectancy by Income Quartile



Source: The Journal of the American Medical Association

While some experts have warned about the potentially adverse effects that increasing the retirement age could have on some subpopulations currently not seeing improvements in overall life expectancy, others have brought attention to other costs associated with this policy, particularly to the impact this policy could have on total retirement benefits received by program beneficiaries.

Kathryn Moore of the University of Kentucky's College of Law conducted a cost-benefit analysis to identify any major costs associated with raising social security retirement ages, as well as any major benefits. She concluded that this

²⁴ Gary Burtless, "Should Congress raise the retirement age to 70?", The Brookings Institution, (June, 2016), <https://www.brookings.edu/articles/should-congress-raise-the-full-retirement-age-to-70/>, (accessed March 5, 2018)

change in policy could reduce the long-term deficit in the Social Security trust fund, and could likely produce general economic gains. Nevertheless, she also identified three major risks worth mentioning. First, increasing the retirement age would constitute a reduction in benefits, as retirees would only be eligible to collect full benefits later in life. Second, Moore believes that older workers may end their lives in poverty as a result. And third, her study also concludes that increasing the retirement age could have a disproportionately adverse impact on workers who are more vulnerable to poverty in old age (i.e. blue-collar workers, low-income workers, African-Americans, etc.).²⁵

b. Raising Cap on Maximum Taxable Earnings

Raising the cap on how much of an individual's total yearly earnings can be subject to the Social Security payroll tax is another critical part of the policy proposal and it is aimed at ensuring that the Social Security Administration has enough resources to cover the program's growing expenses.

This policy change, which would set the cap on the maximum amount of taxable earnings at \$245,000 (currently set at \$128,400), could be very effective at achieving the proposal's goal of ending Social Security's financial shortfall. A study by the Congressional Budget Office indicated that this option could increase revenues by an estimated \$648 billion over the next decade.²⁶ Some have estimated that raising the cap on maximum taxable earnings could close about a quarter of the

²⁵ Kathryn L. Moore, "Raising the Social Security Retirement Ages: Weighing the Costs and Benefits", University of Kentucky, (2001), https://uknowledge.uky.edu/cgi/viewcontent.cgi?article=1114&context=law_facpub (accessed March 5, 2018)

²⁶ Congressional Budget Office, "Increase the Maximum Taxable Earnings for the Social Security Payroll Tax", (December, 2016) <https://www.cbo.gov/budget-options/2016/52266> (accessed March 9, 2018)

program's long-term shortfall.²⁷ While this initiative would add billions in new revenue for the Social Security Administration, most taxpayers won't be affected by the cap being raised since 84% of all wages are already below the current maximum. Under this initiative, the taxable share of earnings from jobs covered by Social Security would increase to 90%, or 6 percentage points.²⁸ Therefore, it would seem that there is strong case to support the cost-effectiveness or efficiency of this option, especially considering the fact that the vast majority of workers currently paying the Social Security payroll tax won't be impacted by this new policy in any way.

In terms of its potential impact on equality, this initiative would be less regressive than the current system. This is because people earning more than the current \$128,400 threshold are paying a smaller percentage of their income into Social Security than those workers whose earnings fall below that threshold. Under the new system, median tax increases would be progressive up to the top 5% of earners. The very highest earners would see smaller tax increases because the cap would not be eliminated altogether.²⁹

Despite this policy's effectiveness and efficiency at potentially accomplishing the proposal's set goals, increasing the maximum taxable earnings is not without its drawbacks. According to the Congressional Budget Office, this new policy could undermine the existing relationship between the amount of taxes workers pay into Social Security and the amount of benefits they receive after retirement. More specifically, the CBO argues that while benefits would increase for those being taxed

27 Kathleen Romig, "Increasing Payroll Taxes Would Strengthen Social Security", Center on Budget and Policy Priorities, (September 27, 2016) <https://www.cbpp.org/research/social-security/increasing-payroll-taxes-would-strengthen-social-security> (accessed March 9, 2018)

28 Congressional Budget Office, "Increase the Maximum Taxable Earnings for the Social Security Payroll Tax"

29 Kathleen Romig, "Increasing Payroll Taxes Would Strengthen Social Security",

a higher percentage of their income under the new cap, that increase would be rather modest in comparison to the amount being paid in new taxes. Furthermore, the substitution effect could kick in as people whose earnings would fall under the new threshold may choose to use part of their time performing other activities that don't involve taxable work hours.³⁰

c. Modifying the Cost of Living Adjustments (COLAs) Formula

The final portion of this policy proposal package involves indexing COLAs to 1-percentage point below the Consumer Price Index (CPI) in a given year, thus offering a more conservative approach to the current formula, which equates COLAs to CPI. This option could be very effective at improving Social Security's solvency. According to the Social Security Administration, the one-point COLA reduction, which would reduce scheduled benefits, could have a significant effect on the system's solvency, potentially fixing 77% of the program's long-range actuarial imbalance.³¹ As these findings show, the effects of COLA reductions could be substantial. And, considering the magnitude of the SSA's forecast and the minimum costs involved in implementing this option, the policy's efficiency would seem evident. Nevertheless, there seems to be widespread agreement among policy annalists that reductions in COLA benefits could lead to higher poverty rates.

The SSA warns that this policy could have potentially negative effects on the poverty rate, especially as it relates to older retirees. Table 4 illustrates the effects of three different COLA-related policy options, which include the 1-percentage point reduction proposed in this memorandum.

³⁰ Congressional Budget Office, "Increase the Maximum Taxable Earnings for the Social Security Payroll Tax"

³¹ Anya Olsen, "Distributional Effects of Reducing the Cost-of-Living Adjustments", Social Security Administration, (November, 2008), <https://www.ssa.gov/policy/docs/policybriefs/pb2008-03.html> (accessed March 9, 2018)

Table 4: Poverty Rate (in percent) by Age Group and Policy Option

Age group	Scheduled benefits	Policy option			Payable benefits	Average length of benefit receipt (years)
		Chained-CPI	Half-point	One-point		
62–69	0.6	0.7	0.7	0.9	2.1	5.1
70–79	0.6	0.7	0.7	1.0	1.9	12.7
80–89	0.6	0.7	1.0	1.6	2.8	22.1
90 or older	0.5	0.9	1.2	2.0	2.1	33.6

Source: Social Security Administration

As the table shows, a 1-percentage point reduction in COLA benefits could quadruple the poverty rate among beneficiaries 90 years old or older, pushing the poverty rate from 0.5 percent under scheduled benefits to 2.0 percent. Poverty rates disproportionately impact the oldest retirees because, as Richard Johnson of The Urban Institute indicates, Social Security has become their primary source of income, whereas younger groups are more likely to have a more diverse income portfolio, which may include pension plans, owned assets, or other earnings, and less likely to solely depend on Social Security for retirement benefits.³²

Older retirees would not be the only group where poverty rates could rise as a result of a redesigned COLA benefits formula. African-Americans, unmarried beneficiaries, or those with less than 12 years of education could also be in danger of falling into poverty, as Social Security continues to represent the largest share of total income among these groups, making them more susceptible to any changes to the benefits formula.³³

³² Richard W. Johnson, “The Distributional Implications of Reductions in Social Security COLAs”, The Urban Institute, (June, 1999), <https://www.urban.org/sites/default/files/publication/66186/309221-The-Distributional-Implications-of-Reductions-in-Social-Security-COLAs.PDF> (accessed March 9, 2018)

³³ Anya Olsen, “Distributional Effects of Reducing the Cost-of-Living Adjustments”

Political Analysis

Understanding the potential implications of this policy proposal from a policy standpoint is a crucial step before any decision on the matter is made. However, being aware of any political implications that may come about as a result of this policy package's implementation is equally important. Therefore, the following pages will offer a detailed analysis aimed at discerning how different political actors and other relevant stakeholders are likely to respond to such proposal, providing ample evidence of their various views on the three main pillars of the policy proposal package.

a. Increasing the Retirement Age

Gradually increasing the retirement age from 67 to 68 between 2027 and 2033 is a proposal traditionally supported by conservative lawmakers and it would likely be well received by Republican leaders in the U.S. Congress. In December of 2016, chairman of the House Ways and Means Subcommittee on Social Security Rep. Sam Johnson proposed a very similar approach that would increase the retirement age to 69 as stipulated in the Social Security Reform Act of 2016, which he sponsored.³⁴ Nevertheless, the proposal may still be deemed as rather bold considering the fact that Republicans and Democrats alike have traditionally kept their distance when it comes to a potential overhaul of Social Security since it remains a widely popular federal program. Furthermore, according to Andrew Soergel of U.S. News Republican leaders have broadly promised that they wouldn't go ahead with legislation that could lead to cuts in benefits for current retirees or soon-to-be

³⁴ The Associated Press, "Republicans propose raising the retirement age, other changes to Social Security", News 10, (December, 2016), <http://news10.com/2016/12/13/republicans-propose-raising-the-retirement-age-other-changes-to-social-security/>, (accessed March 16, 2018)

retirees.³⁵ However, the guidelines put forth by this memorandum's proposal fit into the rhetoric of high profile Republican leaders like Senator Marco Rubio, who recently stated that Social Security should be restructured in a way that "doesn't impact current retirees, but rather in a way that would probably impact it for me and people younger than me".³⁶

Unlike their Republican counterparts, the Democratic Party has occasionally shown stronger signs of divisions on this particular issue. Leading Democratic leaders in the U.S. Senate have often shown sympathy for a possible increase in the retirement age. In 2011, Senators Diane Feinstein, Tom Carper, and Mark Warner all agreed that considering pushing the retirement age beyond 67 should be on the negotiating table.³⁷ However, more liberal Democratic leaders, namely Senators Elisabeth Warren and Bernie Sanders, strongly oppose this move and have often tried to drive the conversation away from raising the retirement age and focus it on potential tax increases.³⁸

Understanding the dynamics at play in the two major political parties in the country is crucial in order to make an informed decision on this policy proposal, but taking into consideration the views of significant interest groups and those of the public at large is just as relevant.

As the nation's leading advocate for senior citizens with a membership that surpasses the 37-million mark, the American Association of Retired Persons (AARP)

35 Andrew Soergel, "After Tax Overhaul, GOP Sets Sights on Medicare, Social Security", U.S. News, (December, 2017), <https://www.usnews.com/news/economy/articles/2017-12-07/after-tax-overhaul-gop-sets-sights-on-medicare-social-security>, (accessed March 16, 2018)

36 Andrew Soergel, "After Tax Overhaul, GOP Sets Sights on Medicare, Social Security",

37 Alexander Bolton, "Some Senate Dems willing to consider Social Security reforms", The Hill, (April, 2011), <http://thehill.com/homenews/senate/155675-some-senate-democrats-are-willing-to-consider-social-security-reforms>, (accessed March 16, 2018)

38 Eric Garcia, "Democrats No Longer Divided On Social Security", Roll Call, (September, 2016), <https://www.rollcall.com/politics/democrats-no-longer-divided-over-social-security> (accessed March 16, 2018)

and their stance on Social Security reform options should be reviewed in this section in more detail. AARP has traditionally opposed any legislation that could entail benefit reductions for Social Security beneficiaries and has often actively participated in campaigns to fight Social Security benefit cuts. Nevertheless, increasing the full retirement age is an area where AARP has, from time to time, opened the door for potential negotiations. In a 2011 interview with CNN, AARP legislative policy director David Certner suggested that raising the age at which retirees begin receiving full Social Security benefits would be on the table during reform negotiations even though he believed such move would represent “a massive benefit cut”.³⁹ It is interesting to note that AARP’s position on this issue matches that of more moderate Democrats and isn’t necessarily in direct opposition with what Republican lawmakers have advocated, an indication that compromise on this portion of the policy proposal may be possible to achieve.

Public opinion in general has voiced a stronger, clearer opposition to increasing the retirement age. A Gallup poll run every five years and last published in 2010 found that 63% of Americans believed increasing the age at which people are eligible to receive full retirement benefits was a bad idea, a percentage unchanged from their 2005 poll.⁴⁰ A slightly more recent poll by Pew Research, however, found that 56% oppose increasing the age of retirement, a considerable drop but still a number representing a solid majority of the American public.⁴¹

³⁹Arthur Delaney, “AARP Willing to Negotiate on Social Security Retirement Age”, Huffington Post, (June, 2011), https://www.huffingtonpost.com/2011/06/17/aarp-social-security_n_878966.html, (accessed March 18, 2016)

⁴⁰Jeffrey Jones, “Americans Look to Wealthy to Help Save Social Security”, Gallup, (July, 2010), <http://news.gallup.com/poll/141611/americans-look-wealthy-help-save-social-security.aspx> (accessed March 18, 2018)

⁴¹David Madland, “Polling Shows Americans Want Retirement Policy Reform”, Center for American Progress Action Fund, (January, 2014), <https://www.americanprogressaction.org/issues/economy/reports/2014/01/30/83193/polling-shows-americans-want-retirement-policy-reform/>, (accessed March 18, 2018).

b. Raising Cap on Maximum Taxable Earnings

Setting the cap on the maximum amount of taxable earnings at \$245,000 for those individuals paying into Social Security represents a new scenario where the tables are turned, having Democrats generally in favor of the proposal and Republicans against it. In 2013, Democratic Senator Tom Harkin sponsored legislation to remove the cap altogether, arguing that the current system is “regressive” and places most of the tax burden on low-income Americans. Sen. Warren and other leading Democrats in the Senate favored the proposal.⁴² On the other hand, Republicans view any such proposal as a tax increase, and according to the GOP’s platform on Social Security the party opposes tax increases and believes in “the power of markets to help save the future” of the program.⁴³

Regarding how interest groups may react to this portion of the policy proposal, AARP has been less hesitant when defining their position on raising the amount of income subject to Social Security payroll taxes. The advocacy organization openly favors raising the current cap as a potential solution to the program’s financial shortfall, stating, “Those who have benefited from the growth in the economy should be asked to pay a little more to help secure Social Security”.⁴⁴

Public opinion has also expressed a clear stance in favor of changes to the current tax structure so that high-income earners have their full wages subject to the Social Security tax. A survey conducted by the National Academy of Social

⁴² David Welna, “To Fix Social Security, Some Democrats Want To Lift Wage Cap”. NPR, (December, 2013), <https://www.npr.org/2013/12/05/249068448/to-fix-social-security-some-democrats-want-to-lift-wage-cap> (accessed March 21, 2018)

⁴³ GOP, “Republican Platform: Government Reform”, <https://gop.com/platform/reforming-government/> (accessed March 21, 2018)

⁴⁴ David John, “Raising the Social Security Payroll Tax Cap Does Not Fix Social Security”, The Heritage Foundation, (February, 2005) https://www.heritage.org/social-security/report/raising-the-social-security-payroll-tax-cap-does-not-fix-social-security#_ftn1 (accessed March 21, 2018)

Insurance explored the possibility of eliminating the taxable earnings cap and how Americans would view such proposal. Now, while that is not what this memorandum's proposal suggests, the survey offers insights into a similar policy that can very well be used to determine how the American public may feel about simply raising the cap. The results of the survey are summarized in the table below.

Table 5: Public Opinion and the Social Security Tax Cap

<i>Responses</i>	<i>Eliminate the taxable earnings cap</i>
Favor	68%
Strongly	39
Somewhat	28
Not sure	24
Oppose	8
Strongly	4
Somewhat	5

Source: National Academy of Social Insurance

With 68% of the American public in favor of eliminating the taxable earnings cap, it should be expected that a large majority of Americans would react positively to any proposal that brought raising the current at \$128,400 cap to \$245,000 to the table.

d. Modifying the Cost of Living Adjustments (COLAs) Formula

This final section of the analysis will explore how political parties, interest groups, and the general public are expected to view modifications to the COLA formula that would index COLAs to 1-percentage point below the Consumer Price Index (CPI). This change to the current formula, which equates COLAs to CPI, would

essentially mean a reduction in COLA benefits, though not a reduction in earned benefits, and Congressional Republicans have occasionally explored the possibility of making COLA benefits more austere.⁴⁵ More specifically, current Senate majority leader Mitch McConnell has often brought up the idea of seeking reductions in cost-of-living adjustments to Social Security recipients during budget talks with the Executive branch.⁴⁶ The Democratic Party, on the other hand, is less likely to support this third pillar of the policy proposal. In 2013, the Obama administration proposed a lighter approach to modifying the COLA formula, the so-called “chained CPI”, though it would have produced smaller benefit increases nonetheless. President Obama had to drop his chained CPI proposal from his budget following fierce opposition from his party.⁴⁷ Consequently, a similar reaction from Democratic leaders should be expected if this proposal were to be brought before Congress, specially considering the fact that the “COLA minus 1” approach proposes an even more conservative definition for the COLA benefits formula.

AARP has also come out strongly against any cuts to COLA benefits every time these have been suggested by policymakers, stating that their organization “will fight any cuts that are proposed to Social Security, including proposals to reduce the cost of living adjustment for beneficiaries (COLA)”.⁴⁸ As an organization representing the interests of tens of millions of seniors and retirees, their stance on

45 Sean Williams, “The GOP tax plan could negatively affect your Social Security benefits”, USA Today, (November, 2017) <https://www.usatoday.com/story/money/personalfinance/retirement/2017/11/23/the-gop-tax-plan-could-negatively-affect-your-social-security-benefits/107865406/> (accessed March 26, 2018)

46 Manu Raju, “Sources: McConnell floats entitlement changes in high-stakes fiscal talks”, CNN, (October, 2015), <https://www.cnn.com/2015/10/13/politics/mitch-mcconnell-entitlement-changes-fiscal-talks/index.html> (accessed March 26, 2018)

47 Jeanne Sahadi, “Obama drops controversial Social Security proposal”, CNN Money, (February, 2014), <http://money.cnn.com/2014/02/20/news/economy/obama-social-security-chained-cpi/index.html> (accessed March 26, 2018)

48 Tina Johnson-Marcel, “AARP CEO Responds to Obama's Deficit Reduction Proposal”, AARP, (July, 2011), <https://www.aarp.org/politics-society/government-elections/info-07-2011/aarp-responds-obama-deficit-reduction-plan.html> (accessed March 26, 2018)

this issues should not come as a surprise, and so their opposition to the “COLA minus 1” plan should be expected.

In simple terms, this last portion of the policy proposal represents a reduction of federal spending on Social Security, and a recent survey by the Pew Research Center found that an overwhelming majority of Americans don’t support decreasing federal spending on Social Security or on most government programs for that matter. In fact, only 3% of Democratic voters and 10% of Republican voters would favor reducing Social Security spending.⁴⁹ With these numbers in mind, it could certainly be a challenge to make the proposed COLA benefits formula appealing to the general public.

The Social Security Administration is aware of the challenges facing the program and has discussed in great detail numerous possible solutions, including some very similar to the ones offered in this paper.⁵⁰ Consequently, and while understanding the limitations of the office in terms of its decision-making powers, the Office of the Acting Commissioner is in a good position to advocate for reform within the current administration in order to bring attention to the issue at hand.

Recommendation

The policy proposal presented in this paper offers a comprehensive approach to addressing a very complex issue. The facts have shown that in a few years Social Security won’t have enough resources to meet the program’s responsibilities and millions of retired Americans could be in danger of losing a crucial source of their

⁴⁹ John Gramlich, “Few Americans support cuts to most government programs, including Medicaid”, Pew Research Center, (May, 2017), <http://www.pewresearch.org/fact-tank/2017/05/26/few-americans-support-cuts-to-most-government-programs-including-medicaid/> (accessed March 26, 2018)

⁵⁰ Stephen Goss, “The Future Financial Status of the Social Security Program”, Social Security Administration, (2010), <https://www.ssa.gov/policy/docs/ssb/v70n3/v70n3p111.html> (accessed April 5, 2018)

income. Therefore, immediate action is necessary if the administration wants to preserve the government's most important social insurance program.

The policy analysis showed that gradually increasing the retirement age to 68, raising the payroll tax cap to \$245,000, and redesigning the benefits formula so that COLAs are indexed to one point below the annual CPI could have a very positive impact on Social Security's financial stability and could ensure the program's financial soundness well into the future. There are concerns that making changes to the retirement age and to the benefits formula could have a negative impact on current beneficiaries, and while there is some truth to that, I believe that the contributions of these two policies to making Social Security more solvent outweigh their downsides. Americans are in fact living longer and increasing the retirement age is a simple adjustment that has happened before and should happen naturally in the future. As for the way the government calculates cost-of-living adjustments, I believe that while my proposal could partially take away COLA benefits from current and future retirees, the current formula is simply too generous and doesn't offer a realistic response when the cost of living goes up. This is because the CPI provides a simplistic view on the cost of living by looking at the average change in price for a specific basket of goods and it doesn't take into consideration the substitution effect. Also, it is important to note the distinction between earned benefits and COLA benefits. If this proposal were to move forward, American retirees would still have their earned benefits guaranteed by law. This would only affect the extra amount that they receive in COLA benefits on an annual basis.

From a political standpoint, the diversity of viewpoints is evident and not everyone will be happy with every single provision presented in this policy package. Nevertheless, it is fair to say that these proposals include some policy ideas traditionally backed by Republicans and others traditionally supported by Democrats. Social Security reform would be impossible if only one of the two major parties was interested in moving this proposal forward. Widespread consensus is needed and the diverse policy profile of this proposal intends to accomplish just that. Public opinion may prove harder to sway, but it is important to remember that addressing Social Security's solvency issues is an urgent matter that requires a bold response from Congress and the administration. The Social Security program requires drastic changes and no single policy proposal will ever be well received by everyone, so only two choices remain: leave it as it is and wait for the program to run out of funds, or make certain sacrifices today so that future generations can continue to enjoy their Social Security benefits throughout their old age.

Therefore, and after careful consideration of the analysis presented in this memorandum, I recommend that you, as Acting Commissioner of the Social Security Administration, approve the proposed policy initiative as stipulated and initialize an organized effort by the administration to work with Congress in the upcoming weeks in order to begin the authorization of a series of reforms which, I believe, will prove crucial in ensuring the long-term financial stability of Social Security. I admit that some of the toughest regulations such as reducing COLA benefits could have detrimental effects on some program beneficiaries in the short-term. However, this

proposal is designed to guarantee the long-term stability of Social Security, which is and should always be your office's number one priority.

Curriculum Vitae

Cesar Lardies Rivas was born on October 3, 1991 and grew up in Torla, Spain. At age 16, Cesar left his home country to attend his High School senior year in Auburn, Washington. He went on to receive a Bachelor of Arts degree in Political Science from George Washington University, where he graduated Magna Cum Laude in 2013. Currently a full-time graduate student, Cesar possesses a very diverse professional profile, which includes internships at the Progressive Policy Institute and at the US Congress, his experience as a teacher and consultant for a language academy in China, as well as his short period as a consultant for the Inter-American Development Bank. Cesar is a candidate for a Master of Arts in Public Management at Johns Hopkins University.